BILL FLORES, CHAIRMAN

RSC THE REPUBLICAN STUDY COMMITTEE

H.R. 1675—Capital Markets Improvement Act of 2016 (Rep. Hultgren, R-IL)

CONTACT: Jennifer Weinhart, 202-226-0706

FLOOR SCHEDULE:

Scheduled for consideration on February 3, under a structured rule.

TOPLINE SUMMARY:

The Rules Committee print of H.R. 1675 includes the texts H.R. 1675 as reported by the Committee on Financial Services as well as the text of H.R. 686, Small Business Mergers, Acquisitions, Sales, and Brokerage Simplification Act of 2015, H.R. 1965, Small Company Disclosure Simplification Act, H.R. 2354, Streamlining Excessive and Costly Regulations Review Act and H.R. 2356, Fair Access to Investment Research Act of 2015.

H.R. 1675, as reported, would increase from $5 million to $10 million the annual amount of securities a firm may sell for employee compensation without requiring additional disclosures pertaining to compensatory benefit plans and other financial information.

H.R. 686 would amend the Securities Exchange Act of 1934 to exempt certain merger and acquisition brokers who advise small businesses in their sales from registration requirements.

H.R. 1965 would exempt certain emerging growth companies and issuers with annual gross revenues of less than $250 million from requirements to use the Extensible Business Reporting Language (XBRL) for financial statements and other mandatory reporting requirements with the Securities and Exchange Commission. These companies would be allowed to use XBRL if they chose to do so.

H.R. 2354 would require the SEC, within 5 years following enactment, and every ten years following, to review every significant regulation it has issued and determine whether it has become unnecessary or overly burdensome, solicit public comment on whether it should be repealed or amended, and repeal or amend any regulation accordingly.

H.R. 2356 would direct the SEC to revise a regulation to create a safe harbor for research reports on exchange traded funds (ETFs) so that the reports are not considered offers under the Securities Act of 1933, but also clarify the law so that broker-dealers can publish research on ETFs.

COST:

The Congressional Budget Office (CBO) estimates that implementing H.R. 1675, as reported, would cost less than $500 thousand over the FY 2016-2020 period.

CBO estimates implementing H.R. 686 would result in an insignificant net budgetary effect.

CBO estimates that implementing H.R. 1965 would cost less than $500k over the FY 2016-2020 period.

CBO estimates that implementing H.R. 2354 would cost less than $500k over the FY 2016-2020 period.

CBO estimates that implementing H.R. 2356 would cost $2 million over the FY 2016-2020 period.

CONSERVATIVE CONCERNS:

There are no substantive concerns.

- **Expand the Size and Scope of the Federal Government?** No.
- **Encroach into State or Local Authority?** No.
- **Delegate Any Legislative Authority to the Executive Branch?** No.
- **Contain Earmarks/Limited Tax Benefits/Limited Tariff Benefits?** No.

DETAILED SUMMARY AND ANALYSIS:

According to the Committee Report, in 1988 the SEC issued Rule 701, to allow private companies to sell securities to employees as compensation. Later, it added disclosure requirements for sales over $5 million in a 12-month period. Rule 701 allows private companies to offer their securities in written compensation, without having to comply with federal securities registration requirements.

Title I would increase the threshold of the aggregate amount of securities exempt from disclosure requirements from $5 million to $10 million during a 12 month period, indexed for inflation every five years. The SEC would have 60 days to increase the threshold following enactment. By giving relief from disclosure requirements, employees of startups will be able to take advantage of the JOBS Act employee shareholder provision, which provides private companies with the ability to purchase company securities to increase employee ownership. This enables companies to keep their employees without having to borrow money or sell securities.

Title II includes the text of the Fair Access to Investment Research Act. Under present law, the SEC prohibits an issuer from offering securities for sale unless a registration statement is filed with the agency. Exchange Traded Funds (ETFs) are investment vehicles, similar to mutual funds, whose shares are traded intraday on exchanges with market-determined prices. Though investor interest in ETFs has grown exponentially, there are anomalies in the SEC's safe harbor rules that have served to discourage broker-dealers from publishing research reports on ETFs.

Section 201 would, within 45 days following enactment, require the SEC to propose and adopt revisions to section 230.139 of title 17 of the Code of Federal Regulations regarding safe harbor, to provide that a covered investment research fund report does not constitute an offer for sale or an offer to sell. This would not be conditioned upon whether, in the case of covered investment funds with a class of securities in substantially continuous distribution, the broker or dealer's publication is an initiation or re-initiation of research coverage on a covered investment fund or its securities.

To qualify for safe harbor, a broker or dealer would be required to distribute a research report in the regular course of business, which relates to an Exchange Traded Fund issue "that: (1) has a class of securities listed on a national securities exchange for at least 12 months prior to the publishing or distribution of the report, (2) has an aggregate market value of at least $75 million; and (3) is either a unit investment or an open-ended company or a trust whose assets consist primarily of interests in commodities, currencies, or derivative instruments referring commodities or currencies.[1]"

[1] House Report 114-401

In implementing safe harbor, the SEC would not be able to require the covered investment fund to have been registered as an investment company under the Investment Company Act of 1940 or be subject to reporting requirements under the Securities Exchange Act of 1934, nor would they be able to impose a minimum threshold for the number of traded share in excess of that in title 17 of the Code of Federal Regulations.

This section would provide that a self-regulatory organization may not enforce any rule that would condition a member's ability to publish a research report on whether they are also participating in a registered offering or distribution of any securities or condition the ability of a member to participate in a registered offering or securities distribution on whether they have published a research report on such a covered investment report of its securities. A covered research report would not be subject to sections 24(b) or 34(b) of the Investment Company Act.

If the SEC does not revise the rule within 45 days to implement the legislation, this section would provide an interim safe harbor.

Title III includes the text of the Small Business Mergers, Acquisitions, Sales, and Brokerage Simplification Act. Mergers and acquisitions (M&A) brokers provide essential services to small businesses wanting to sell or merge with other businesses to grow. This legislation would help to eliminate complicated and counterproductive regulations that require registration of certain M&A brokers. This legislation would exempt M&A brokers from registration requirements under the Securities and Exchange Act of 1934, so long as brokers do not undertake an excluded activity. Brokers not eligible for exemption would include those who: (1) receive, hold, transmit or have custody of securities or funds that will be exchanged by parties to an ownership transfer of an eligible privately held company; or (2) who engage on behalf of an issuer in a public offering of security that require mandatory registration, or if the issuer must file information, documents, and reports. This legislation would be required to take effect within 90 days after enactment.

Title IV includes the text of the Small Company Disclosure Simplification Act. According to the Committee Report, the final report of the SEC's Government-Business Forum on Small Business Capital Formation recommends the elimination of the reporting requirements for small companies to submit financial information in XBRL format for SEC filings, as the requirements impose additional burdens on small businesses that don't yield benefit to investors. XBRL is a specific data format in which each data item is tagged uniquely to be easily manipulated by users.

In the 113th Congress, the Financial Services Committee passed identical legislation, H.R. 4164, out of Committee 51-5.

Section 401 would exempt small companies with less than $250 million in revenues and emerging growth companies from XBRL requirements for financial statements and other periodic reports to the SEC. This exemption would run for five years following enactment, unless the SEC determines the benefits of XBRL reporting outweigh the costs. If this determination is made, the exemption would run for two years following the determination.

Section 402 would require the SEC to conduct a cost benefit analysis of smaller companies using XBRL.

Section 403 would require the SEC to submit a report to Congress within 1 year of enactment on the implementation and use of XBRL reporting and the results of the Section 3 analysis.

Title V includes the text of the Streamlining Excessive and Costly Regulations Act. This legislation would require the SEC, within five years following enactment, and every ten years thereafter, to review each significant regulation issued by the commission and determine whether each regulation is outdated,

unnecessary, or overly burdensome, and provide notice and solicit comment on each regulation to determine if it should be amended or repealed. The SEC would then be required to amend or repeal regulations as determined by the commission pursuant to the determination. This Title would also require the SEC to submit a report to Congress within 45 days following each determination. Any vote by the Commission would not be subject to judicial review.

Committee reports for the text can be found here, here, here, here, and here.

AMENDMENTS:

1. Ellison (D-CA) 1 – This amendment would strike the text of H.R. 1965 (Title IV).
2. Ellison (D-CA) 2 – This amendment would narrow the Title IV exemption to emerging growth companies, and only for a period of three years. It would nullify the exemption if the SEC permits corporations to file using inline XBRL formatting.
3. Issa (R-CA), Polis (D-CO) – This amendment would leave the Title IV XBRL reporting exemption for Emerging Growth Companies intact, while decreasing the exemption for other small companies from five years to two years. It would allow the SEC to cancel the exemption within 180 days, rather than two years, if a cost-benefit analysis shows the benefits of XBRL reporting outweigh the costs.
4. Issa (R-CA), Polis (D-CO) 2 – This amendment would limit all exemptions granted under Title IV to new companies that had not previously been required to file in XBRL format.
5. Huizenga (R-MI) – This amendment would clarify the disqualification from exemption under Title III of any broker or associated person that is subject to suspension or revocation of registration, and the inapplicability of the exemption when one or more parties to an M&A transaction is a shell company.
6. Sherman (D-CA) – This amendment would provide exclusions for when an M&A broker is not exempt from registration with the SEC under Title III. Exclusions would include brokers that have been barred by the SEC, state, or other self-regulatory organization, or to any transactions involving shell companies, and others.
7. DeSaulnier (D-CA) – This amendment would direct the SEC to submit a report to Congress on the prevalence of employee ownership plans within companies that include a flexible or social benefit component in their articles of incorporation.

COMMITTEE ACTION:

H.R. 1675 was introduced on March 26, 2015 and was referred to the House Committee on Financial Services, where it was reported on May 20, 2015.

H.R. 686 was introduced on February 3, 2015, and was referred to the House Committee on Financial Services where it was reported on May 20, 2015.

H.R. 1965 was introduced on April 22, 2015, and was referred to the House Committee on Financial Services where it was reported on May 20, 2015.

H.R. 2354 was introduced on May 15, 2015, and was referred to the House Committee on Financial Services where it was reported on May 20, 2015.

H.R. 2356 was introduced on May 15, 2015, and was referred to the House Committee on Financial Services where it was reported on May 20, 2015.

ADMINISTRATION POSITION:

A Statement of Administration Policy can be found here.

CONSTITUTIONAL AUTHORITY:

According to the sponsor, Congress has the power to enact H.R. 1675 pursuant to Article I, Section 8, clause 3, Article I, Section 8, clause 18 of the United States Constitution.

According to the sponsor, Congress has the power to enact H.R. 686 pursuant to Article I, Section 8, clause 1, Article I, Section 8, clause 3, Article I, Section 8, clause 18 of the United States Constitution.

According to the sponsor, Congress has the power to enact H.R. 1965 pursuant to Article I, Section 8, clause 3 of the United States Constitution.

According to the sponsor, Congress has the power to enact H.R. 2354 pursuant to Article I, Section 8, clause 3, Article I, Section 8, clause 18 of the United States Constitution.

According to the sponsor, Congress has the power to enact H.R. 2356 pursuant to Article I, Section 8, clause 3 of the United States Constitution.

NOTE: *RSC Legislative Bulletins are for informational purposes only and should not be taken as statements of support or opposition from the Republican Study Committee.*